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Adams, J. Frank

Collateral inheritance taxation

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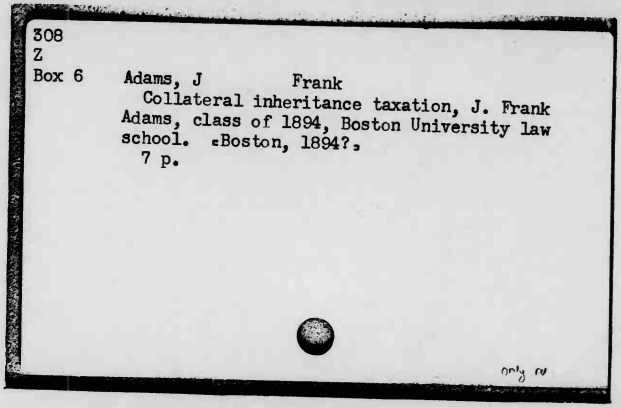

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COLLATERAL INHERITANCE TAXATION.

J. FRANK ADAMS.

CLASS OF 1894.
BOSTON UNIVERSITY LAW SCHOOL.

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1894 ?

Compliments of

J. Frank Adams.

COLLATERAL INHERITANCE TAXATION.

By J. Frank Adams.

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The passage in Massachusetts in 1891 of "An Act imposing a tax on collateral inheritances and successions," the efforts made in 1892 and 1893 to secure its repeal, and the probability that the constitutionality of the law will be tested in a few months in the Supreme Judicial Court of the State, have caused much thought, comment, and discussion, and a brief review of the subject may not prove uninteresting.

Taxes are defined to be "the enforced proportional contributions from persons and property, levied by the State by virtue of its sovereignty for the support of government, and for all public needs."[1]

It is said that taxation is an equal division of the public expense,[2] but it is manifestly practically impossible to assess taxes with perfect equality.

The true principle of taxation is, that each individual of the community should contribute toward the support of the government only a reasonable share of the burden in proportion to the value of the property owned and the privileges enjoyed by him. In levying taxes regard should be had to the question whether or not they will affect the rich and the poor substantially alike, because "a tax on breadstuffs exclusively," for instance, "would . . . compel unequal contributions . . . by means of the necessities of the poor."[3]

The collateral inheritance tax is spoken of as one "of great antiquity, having been imposed by the Romans as early as the days of the Emperor Augustus."[4] It is now in force in England as well as in thirteen of the United States, and in a number of instances has been held to be constitutional;[5] in one State, however, New Hampshire, it has been held to be unconstitutional;[6] the reason for this distinction is to be found in the fact that it was considered to be opposed to the provision in the State Constitution which empowers the Legislature "to impose and levy proportional and reasonable assessments, rates, and taxes upon all the inhabitants of, and residents within the said State, and upon all estates within the same,"[7] and to the Bill of Rights, by which every inhabitant is bound to contribute only his share in the expense of the government.[8] It is said, that "it is not to be questioned that the power to tax is vested in the Legislature; that it is unrestricted except

(1) Cooley on Taxation, p. 1.
(2) State *v.* Express Co., 60 N. H. 219, 237.
(3) Cooley on Taxation, p. 164.
(4) Eyre *v.* Jacob, 14 Grat. 433.
(5) *Id.*; Matter of McPherson, 104 N. Y. 306; Tyson *v.* State, 28 Md. 577; 38 Fed. Rep. 184.
(6) Curry *v.* Spencer, 61 N. H. 624.
(7) Art. 5.
(8) Art. 12.

when it is opposed to some provision of the Federal or State Constitution; that in the absence of constitutional prohibition, the Legislature has the power to impose conditions by way of a tax upon legacies and successions."[1] This latter assumption is based upon the fundamental principle that while man has an inherent and natural right to acquire, possess, and dispose of property during his lifetime, he has no such right to dispose of property by devise, or to take property by descent.[2] That is a mere municipal privilege, and subject to change, modification, or repeal in the discretion of the State.

The decision of the Massachusetts Supreme Judicial Court upon the interpretation of the Constitution of that State, with reference to the collateral inheritance tax, will be of great interest, partly for the reason that the Constitution of New Hampshire is copied largely from that of Massachusetts.

There is, however, a provision in the Massachusetts Constitution which was probably intentionally omitted from the New Hampshire Constitution; the clause referred to empowers the Legislature "to impose and levy reasonable duties and excises upon any produce, goods, wares, merchandise, and commodities, whatsoever, brought into, produced, manufactured, or being within the same."[3] It is probably under this clause that the attempt to uphold the constitutionality of the act will be made in Massachusetts, upon the ground that it is a duty or excise upon a "commodity."

It was decided in Eyre *v.* Jacob,[4] that such a tax was not a tax upon property, but on the privilege of succeeding to the inheritance; and in Portland Bank *v.* Apthorp,[5] that the word "commodity, which signifies convenience, privilege, profit and gains, as well as goods and wares, . . . has been applied by our Legislature . . . to the privilege of using particular branches of business or employment, as the business of an auctioneer, of an attorney, of a tavern-keeper, of a retailer of spirituous liquors, etc."

The question which will next arise will be, whether or not the law is reasonable, inasmuch as it discriminates between the beneficiaries.

Parker, C. J., in Portland Bank *v.* Apthorp,[5] says, "taxes of this sort must undoubtedly be equal; that is, they must operate upon all persons who exercise the employment which is so taxed." By analogy, it would seem that an inheritance or succession tax, in order to be equal and reasonable, should include everybody who is benefited by the distribution of the property, to wit, both direct and collateral heirs and legatees.

In New Hampshire, a law was held unconstitutional which imposed a tax of two per cent on gross receipts, or, in lieu of that, five dollars per mile for the number of miles of railroad over which express business was done, thus impliedly taxing only those who did express business over a railroad, and thereby excepting from its operation those who did express business by some other means of conveyance.[6] In

(1) Curry *v.* Spencer, *supra*.
(2) 2 Bl. Com. 10-13.
(3) Const. of Mass., part 2, Chap. 1, Sect. 1, Art. IV.
(4) 14 Grat. 422.
(5) 12 Mass. 256.
(6) State *v.* Express Co., 60 N. H. 219, 244.

other words, the Supreme Court of New Hampshire has virtually decided, in the cases of State *v.* Express Company,[1] and Curry *v.* Spencer,[2] that the laws which they decided to be unconstitutional were measures of extortion rather than of taxation.

In Portland Bank *v.* Apthorp,[3] a tax on the stock of an incorporated banking company, whose charter existed prior to the passing of the tax law, was held constitutional as being a tax on a commodity. It was especially upon the ground, however, that under that law all the banks would be taxed substantially alike; that there would be no discrimination.

In Oliver *v.* Washington Mills,[4] it was held, that the Legislature has no power to pass a statute requiring corporations to receive and pay into the State treasury a certain portion of all dividends declared by them on the shares of non-resident owners, on the ground that there was a discrimination which was unconstitutional.

In Commonwealth *v.* Five Cents Savings Bank,[5] it was held, that the Legislature has power to impose on savings banks an annual tax on the average amount of deposits; the Court said, "It must be regarded as an excise or duty on the privilege or franchise of the corporation."

In Gleason *v.* McKay,[6] the law was held unconstitutional, in that particular case, because the defendant in the case was not a corporation and enjoyed no franchises conferred on it by the Legislature. "It has constituted its partnership under its common law rights."

In Wallace *v.* Myers,[7] the New York collateral inheritance tax was held not to conflict with the Fourteenth Amendment to the Federal Constitution ("no State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law, nor deny to any person within its jurisdiction the equal protection of the laws"), as the law "operates alike on all property and persons similarly situated." Of course, this court did not pass upon the constitutionality of the State law so far as it referred only to the affairs of that State alone, because the United States Courts are bound to follow and be governed by the decisions of the highest courts of the State in such cases.

In Connecticut Insurance Company *v.* Commonwealth,[8] a tax on the net value of all policies of life insurance corporations in force on a certain day was held constitutional; "the court cannot declare a tax or excise illegal and void as being unreasonable unless it is unequal and contrary to common right." In this case the excise was held not unreasonable, because "it is not unequal, but operates alike upon all corporations or associations which exercise the franchise."

In Commonwealth *v.* Hamilton Manufacturing Co.,[9] it was held, that the Legislature has power to make corporations pay a tax on the

(1) State *v.* Express Co., 60 N. H. 219, 244.
(2) 61 N. H. 624.
(3) 12 Mass. 256.
(4) 11 Allen, 268.
(5) 5 Allen, 428.
(6) 134 Mass. 419.
(7) 38 Fed. Rep. 184.
(8) 133 Mass. 161.
(9) 12 Allen, 298.

excess of the market value of their capital stock, because it is a tax on the franchise.

In Braun *v.* Chicago,[1] it was held, that a license fee or tax, "when imposed on persons engaged in a given business, as that of a broker, whether a produce or grain broker, real-estate broker or insurance broker, . . . is not in violation of any constitutional provision when such fees are uniform as to all persons of the same class."

In another Illinois case,[2] a discrimination as to taxing foreign and domestic insurance companies was upheld, as they are different classes, and foreign corporations have the privilege of doing business in the State "only by the comity which exists between the States."

That this last proposition is not contrary to the Constitution of the United States, see the leading case of Paul *v.* Virginia,[3] in which it was decided that corporations are not "citizens" within the meaning of the same. See also Philadelphia Fire Association *v.* New York.[4]

It is claimed that the right to select subjects for taxation necessarily involves the right to exempt those not selected, and that it is in the discretion and power of the Legislature to determine whether public policy requires such exemption. That is true only so far as the exemption does not infringe on the rights of the people as defined by the Constitution of each particular State.

In Massachusetts, for example, "the personal property of literary, benevolent, charitable, and scientific institutions incorporated within this Commonwealth; all property belonging to common school districts; the wearing apparel and farming tools of every person; his household furniture not exceeding one thousand dollars"; and mechanic's tools to the value of three hundred dollars, are exempt from taxation, among other things, but the exemption applies to all, and not to a part, of those who fall within the class.[5]

It is difficult to see how it can be held constitutional in Massachusetts to tax *some* of the beneficiaries of a devise or inheritance, and exempt others. They are all in the same class, though not always benefited in the same degree.

Although collateral inheritance taxation is not by any means a new and untried thing, yet the active discussion of such a tax in late years has made it a matter of prominence, and has perhaps brought it home to the average man as a comparatively novel matter, and popular interest in it seems to increase rather than to abate.

There seem to be many objections to a collateral inheritance tax, but very few objections to a direct inheritance tax. A direct inheritance tax could be levied so as to afford a large revenue to the State without being burdensome or unjust to even the nearest relatives of the decedent. Such a tax is certainly founded on the broadest principles of equity. It would operate alike on all persons who would enjoy the same privilege or "commodity." It would not fall heavily upon the poor, if the rate per cent and the amount excepted were made reason-

(1) 110 Ill. 186.
(2) Hughes *v.* Cairo, 92 Ill. 339.
(3) 8 Wall. 168.
(4) 119 U. S. 110.
(5) Mass. Pub. Sts., Chap. 11, § 5.

able. If, for instance, the amount exempted was $10,000, and the rate per cent on all estates valued at $10,000 to $500,000 was made one per cent, and a graduated scale per cent upon all estates above $500,000 was made, it would seem to be as near perfection as could reasonably be expected.

No doubt a man has a right to give away anything he owns, but when he does so he deprives himself of its use. By leaving his property to his descendants or to legatees, however, he does not deny himself, but simply controls after death what nature prevents him from governing. Man's natural rights do not extend beyond the grave, and it is against the common good that men shall enjoy the fruits of other men's exertions unearned by themselves, certainly, unless they are willing to pay a comparatively small tax to the State for the privilege accorded them by it, as well as for a just and equitable contribution towards sustaining the expenses of the Probate Courts, which are established and maintained by the State for their benefit and protection, in the proper transfer of the property of decedents.

It is the general opinion that many men, not only the immensely wealthy, but others who are called merely wealthy or well-to-do, conceal the amount of their wealth during their lifetime, and evade the payment of their just and proportional share of the common burden of taxation, and it is doubtless impossible to entirely check the practice; at all events, if not impossible, it is a very difficult problem, and one which has not, apparently, been solved in any country. Under these circumstances, a direct inheritance tax would offset to a large extent the injury done to the people who form the government.

A graduated income tax, it is universally admitted, would be the ideal form of taxation, but it is also admitted that there are many unscrupulous men who would not hesitate to perjure themselves in order to reap the advantages thus gained, to the detriment of the honest and scrupulous.

It seems to be the growing feeling among all fair-minded men, that a collateral inheritance tax does not go far enough, and that a direct inheritance tax ought to be collected, and both the Republican and Democratic parties, in their last conventions in this State, inserted planks in their platforms favoring such a tax.

In England, in 1853, a succession tax was passed, levying a duty on a graded scale, according to the person so taking. Where the successor shall be the lineal issue or lineal ancestor of the predecessor, a duty at the rate of one pound per centum is levied upon the value of the property. If a brother or sister, or a descendant of the same, a duty at the rate of three pounds per centum. And where the successor is remotely connected, or a stranger in blood, a duty of ten pounds per centum.

In New York,[1] in 1885, an act was passed, "to tax gifts, legacies, and collateral inheritances"; it was to the effect, that "all property other than to or for the use of his or her father, mother, husband, wife, children, brother, sister, the wife or widow of a son, the husband of a daughter, or any child or children adopted," should be taxed five dollars on every one hundred dollars, and estates of less than five hundred dol-

(1) Laws of N. Y., 1885, Act 483.

lars were not subject to the same. In 1892,[1] however, another act was passed extending the law to taxation of personal property inherited by direct heirs; this tax amounts to one dollar on every one hundred dollars, on estates valued at more than ten thousand dollars.

The figures showing the amount of money New York has received on account of the tax on inheritances since the laws went into effect make an eloquent showing. They are as follows: —

1886	$84,128.92	1890	$1,117,637.70
1887	561,716.23	1891	890,267.54
1888	736,062.31	1892	1,786,218.47
1889	1,075,692.25	1893	3,071,687.09

This makes a grand total of $9,323,410.51 received in eight years.

It is said that the State of New York collected a tax of more than five hundred thousand dollars on the estate of the late Jay Gould, which was valued at seventy million dollars, although it was not until then ascertained (?) that during his lifetime he was assessed and paid a tax on only five hundred thousand dollars. It is a partial reparation to the State in such a case of evident evasion of taxes during a man's lifetime, that upon his death a complete inventory of his wealth can be made, and a reasonable tax imposed upon the transfer of the property.

In Michigan, in 1893, a law was passed imposing a tax on real and personal property of over five hundred dollars in value. Exemptions as to direct heirs are made, with the exception that the New York law has been followed to a certain extent, and a tax of one per cent imposed on all personal property of more than five thousand dollars in value.

If the present Massachusetts law extended to direct heirs, even though it applied only to the personal property which came to them, the result would probably have been, that in the case of the settlement of the estate of the late Fred. L. Ames, the amount realized by the State would have been in the neighborhood of two hundred and fifty thousand dollars, whereas the probabilities are that the amount collected under the present law will amount only to a few thousands of dollars.

It can hardly be claimed that the payment of even so large a sum as two hundred and fifty thousand dollars would have been unjust or burdensome in the least to the heirs and legatees in this case.

That such taxation is not double taxation is proved by the fact that it is not a tax on property, but on the transfer of property.

In some States a probate fee, graduated according to the value of the estate, and approximating in rate one tenth of one per cent, is collected, and corresponds more or less closely to succession taxes; but this would seem to be a method of "beating about the bush," instead of attempting to solve the problem in a more direct and apparently sensible manner.

Apparently, the practical results in New York would seem to destroy any theoretical objections.

The collateral inheritance tax was probably originally laid with more regard to its being a tax which, on the face of it, would cause less opposition than a direct inheritance tax, than to motives of justness. The

(1) Laws of N. Y., 1892, Chap. 169.

ones upon whom this tax was levied would naturally be comparatively few in number, and their opposition to being singled out from the whole class of legatees could be more easily made to appear to the popular opinion as being based simply on the ground of their selfish desire to evade taxation, than as one really based, on the part of many, on the general principle that taxation should be equal and proportional in its effect as applied to the different forms of taxation which are necessary to the support of every State. The argument, or appearance of an argument, that one to whom property has come in the form of a godsend shows very poor taste, to say the least, in objecting to pay such a tax, is one which it is easy to make, and at first blush would seem unanswerable, especially to those who, thinking that that kind of lightning would never strike them, are content to let the matter rest there and not give any thought or care as to the justness of the objection raised. In the long run, however, the fairness of the objections raised will be more apparent, and justice will prevail.

The State Treasurer of Massachusetts, in his annual report of Dec. 31, 1893, to the Legislature, states that the entire amount collected under the collateral inheritance law up to Dec. 31, 1892, was $13,854.54, and that the amount collected in 1893 was $59,429.31. He goes on to say, "if a tax on collateral legacies and successions is just and equitable, I cannot see why all other legacies and successions are not equally legitimate objects of taxation."

The legislative committee on the revision of the tax laws of Massachusetts have been holding sessions in different parts of the State during the past six months, and several prominent citizens have advocated to them the adoption of a graded succession tax on both direct and collateral inheritances, including bequests to charities, whether public on private.

In Connecticut, the committee of the State Grange on taxation presented their report lately, recommending a graduated distribution tax on estates of deceased persons, and it was unanimously adopted.

In the Congress of the United States, also, in January, 1894, an amendment to a bill was offered by Representative Bynum, of Indiana, to include in the enumeration of income taxation everything received by gift, devise, or inheritance. Representative Springer explained that the adoption of this amendment would bring in a revenue of three or four million dollars a year, and the Gould estate would have paid one million four hundred thousand dollars into the treasury, had the amendment been in force at the time of the deceased's death.

Perhaps the fact that there are so many men at the present day who are possessed of fortunes which run from ten million dollars to one hundred million dollars, and who when death overtakes them are likely to leave the great bulk of their property to their direct descendants, who, under a collateral inheritance tax, would not have to pay anything for the privilege of succeeding to such immense wealth, has had great influence towards shaping legislation in the line of direct inheritance taxation. But at all events, whatever the cause, the chances are good that such legislation will be demanded by the inhabitants of most, if not all, of the United States, within a very few years.

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